

# Inspector General

## United States

## Department of Defense



Oversight Review

September 2, 2011

Report on Failure of Defense Contract Audit Agency,  
Santa Ana Branch Office to Provide Adequate  
Support in Response to a Request for Review of  
Interim Public Vouchers

Report No. D-2011-6-010

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## **Acronyms**

CAM	Contract Audit Manual
DCAA	Defense Contract Audit Agency
DFARS	Defense Federal Acquisition Regulation Supplement
FAO	Field Audit Office
FAR	Federal Acquisition Regulation
MRD	Memorandum for Regional Directors
GAO	Government Accountability Office
IG	Inspector General



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

September 2, 2011

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY

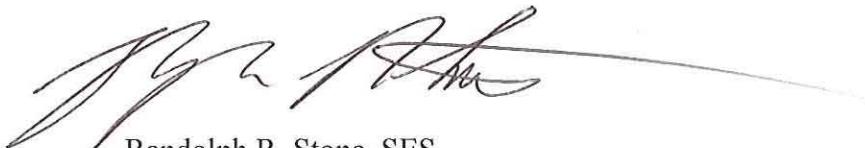
SUBJECT: Report on Failure of Defense Contract Audit Agency, Santa Ana Branch Office, to Provide Adequate Support in Response to a Request for Review of Interim Public Vouchers (Report No. D-2011-6-010)

We are providing this report for review and comment. During our review of a DoD Hotline complaint we identified significant concerns regarding the audit support that the Defense Contract Audit Agency (DCAA), Santa Ana Branch Office, failed to provide in response to the contracting officer's request for a review of interim public vouchers. Our concerns address timeliness in responding to the contracting officer's request, failure to select and review interim public vouchers, and failure to issue a DCAA Form 2000 for suspected irregular conduct or DCAA Form 1 to suspend costs billed by a contractor that is delinquent in paying for accrued costs in the ordinary course of business. On April 14, 2011, we issued a Notice of Concern to the Director, DCAA recommending that the agency take several actions in response to our findings. In preparing this report, we considered management comments in response to the Notice of Concern.

DOD Directive 7650.3 requires that all recommendations be resolved promptly. Please reconsider your nonconcurrence with Recommendation 5. Therefore, we request that the Director of DCAA comment again on Recommendation 5 by October 4, 2011. As a result of management comments, we deleted Notice of Concern Recommendation 6. We renumbered Notice of Concern Recommendation 7 as Recommendation 6 in this report.

If possible, please send a .pdf file containing your comments to [carolyn.davis@dodig.mil](mailto:carolyn.davis@dodig.mil). Copies of the management comments must contain the actual signature of the authorizing official. We are unable to accept the /Signed/ symbol in place of the actual signature.

We appreciate the courtesies extended to the staff. Please direct questions to Ms. Carolyn R. Davis at (703) 604-8877 (DSN 664-8877) or [carolyn.davis@dodig.mil](mailto:carolyn.davis@dodig.mil).



Randolph R. Stone, SES  
Deputy Inspector General  
Policy and Oversight



# Results in Brief: Report on Failure of Defense Contract Audit Agency, Santa Ana Branch Office, to Provide Adequate Support in Response to a Request for Review of Interim Public Vouchers

## What We Did

We reviewed a DOD Hotline complaint concerning allegations of abuse of authority by the contracting office, legal office, and program manager against the complainant. We did not substantiate the complainant's allegations and we issued a Hotline Completion Report. However, during the course of our review, we identified significant concerns regarding audit support that the Defense Contract Audit Agency (DCAA), Santa Ana Branch Office failed to provide in response to the contracting officer's request for a review of interim public vouchers.

## What We Found

We found that DCAA did not respond timely to the contracting officer's request for a review of interim public vouchers. DCAA did not review any of the first 12 interim public vouchers that it approved for payment. DCAA did not submit a DCAA Form 2000, "Suspected Irregularity Referral Form," in accordance with agency policy even though the DCAA Santa Ana Branch Office said it would do so in its September 2009 memorandum to the contracting officer. In addition, DCAA did not submit a DCAA Form 1, "Notice of Contract Cost Suspended and/or Disapproved" when the auditors found that the contractor billed accrued costs that the contractor is delinquent in paying in the ordinary course of business.

## What We Recommend

In April 2011, we issued a Notice of Concern to DCAA recommending several corrective actions to address the reported deficiencies and improve related services. The DCAA Director should review the quality assurance procedures of the DCAA Santa Ana Branch Office for ensuring timely responses to requests; reassess the adequacy of its procedures for reviewing public vouchers; evaluate its procedures and processes for submitting a DCAA Form 2000 and a DCAA Form 1; and reassess the guidance allowing for delegations of signatory authority to the GS-9 auditor level to provisionally approve interim public vouchers. The Santa Ana Branch Office should review an appropriate minimum sample of previously approved interim public vouchers.

## Management Comments and Our Response

The Director, DCAA concurred with 5 of the 7 recommendations in the Notice of Concern. We request that DCAA reconsider its nonconcurrence with Recommendation 5 to reassess the delegation of signature authority and provide additional comments by October 4, 2011. As a result of management comments, we deleted Notice of Concern Recommendation 6. We renumbered Notice of Concern Recommendation 7 as Recommendation 6. Please see the recommendations table on the following page.

## Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Director, Defense Contract Audit Agency	5	1, 2, 3, 4, and 6

**Please provide comments by October 4, 2011.**

# Table of Contents

## Introduction

Objective	1
Background	1

## Finding. Failure to Provide Adequate Audit Support

Background	2
Our Review	3
Notice of Concern, Management Comments, and Our Response	6

## Appendix

A. Scope and Methodology	10
B. DOD Inspector General Notice of Concern	11
C. Defense Contract Audit Agency Comments to Notice of Concern	15

# Introduction

## Objective

We conducted this review to determine whether we could substantiate the allegations received by the DOD Hotline concerning abuse of authority by the contracting office, legal office, and program manager against the complainant. The complainant's allegations were not substantiated and we issued a Hotline Completion Report. During the course of our review, we identified significant concerns regarding audit support that the Defense Contract Audit Agency (DCAA), Santa Ana Branch Office failed to provide in response to the contracting officer's request for a review of interim public vouchers.

See Appendix A for details of our scope and methodology.

## Background

### ***Defense Contract Audit Agency (DCAA)***

While serving the public interest as its primary customer, DCAA performs contract audits for the DOD and provides accounting and financial advisory services regarding contracts and subcontracts to all DOD Components responsible for procurement and contract administration. DCAA operates under the authority, direction, and control of the Under Secretary of Defense (Comptroller)/Chief Financial Officer.

In accordance with DOD Directive 5105.36, DCAA shall audit, examine, and/or review contractors' and subcontractors' accounts, records, documents, and other evidence; systems of internal control; and accounting, costing, and general business practices and procedures in accordance with Government Auditing Standards, the Federal Acquisition Regulation (FAR), the Defense Federal Acquisition Regulation Supplement (DFARS), and other applicable laws and regulations. DCAA shall approve, suspend, or disapprove costs on reimbursement vouchers received directly from contractors, under cost-type contracts, and transmit the vouchers to the cognizant disbursing officer. Also, DCAA shall report incidents of suspected fraud, waste, and abuse to the appropriate authorities.

In accordance with FAR 42.101, the auditor is responsible for (1) submitting information and advice to the requesting activity, based on the auditor's analysis of the contractor's financial and accounting records or other related data as to the acceptability of the contractor's incurred and estimated costs; (2) reviewing the financial and accounting aspects of the contractor's cost control systems; and (3) performing other analyses and reviews that require access to the contractor's financial and accounting records supporting proposed and incurred costs.

# **Finding**

## **Failure to Provide Adequate Support in Response to a Request for Review of Interim Public Vouchers**

We found that the DCAA Santa Ana Branch Office failed to provide adequate support in response to the contracting officer's request for a review of the contractor's interim public vouchers.

### **Background**

On June 11, 2008, the Air Force awarded a cost plus fixed fee contract to the contractor in the amount of \$637,990. On July 3, 2008, the contracting officer issued a Stop Work Order because the Air Force believed that the contractor did not comply with certain contract terms. While in effect, the Stop Work Order prohibited the contractor from incurring additional costs under the contract. The contracting officer lifted the Stop Work Order on September 29, 2008. On November 5, 2008, the contracting officer requested the DCAA Santa Ana Branch Office to review the first 12 interim public vouchers totaling \$130,119 submitted by the contractor under the contract because the contracting officer suspected the vouchers might include costs incurred during the Stop Work Order. DCAA had previously approved the 12 vouchers for payment through the Wide Area Workflow network. DCAA did not review any of the first 12 vouchers that it approved for payment. The contracting officer directed DCAA not to approve any further vouchers for payment pending DCAA's review of the 12 public vouchers.

In a September 11, 2009, memorandum (ten months after the contracting officer's audit request), the DCAA Santa Ana Branch Office informed the contracting officer that it was canceling the review. The DCAA memorandum stated that a review of the public vouchers could not be performed because the contractor failed to provide financial statements, tax returns, certain bank statements, and other requested supporting documents. Nevertheless, the DCAA memorandum identified a significant amount of vendor and subcontractor costs included in the vouchers that the contractor had not paid, prompting the Santa Ana Branch Office to state that it would refer the matter to the Defense Criminal Investigative Service. The DCAA September 11, 2009, memorandum confirmed telephone conversations that occurred on April 30, 2009 between the auditors and contracting officer, and a draft of the memorandum dated May 2009. The content of the May 2009 draft memorandum is identical to the September 11, 2009 memorandum.

At the request of the contracting officer, an investigation was initiated by the Air Force Office of Special Investigations. The investigation confirmed that the contractor used the public voucher payments for personal purposes rather than to pay vendors and subcontractors. As a result, the Government debarred the contractor from future contract awards, and the Air Force is attempting to recover the voucher payments from the contractor.

## Our Review

We interviewed the contracting officer, attorney, and investigator at Hanscom Air Force Base. In addition, we interviewed the supervisory auditor and auditor at DCAA Santa Ana Branch Office. We also reviewed applicable DCAA audit reports regarding the contractor, researched applicable regulations, DCAA Contract Audit Manual (CAM), and DCAA agency policies.

Our review found that DCAA Santa Ana Branch Office failed to:

- respond timely to the contracting officer's request,
- select for review any interim public vouchers prior to approval for payment,
- issue a DCAA Form 2000 for suspected irregular conduct, and
- issue a DCAA Form 1 to suspend costs billed by a contractor that is delinquent in paying for accrued costs in the ordinary course of business.

### ***Timely Response to Contracting Officer's Request***

We found that DCAA Santa Ana Branch Office did not respond timely to the contracting officer's November 5, 2008 request to review the first 12 interim public vouchers submitted by the contractor under the contract. DCAA previously approved these public vouchers for payment. The contracting officer submitted the request because she suspected the interim public vouchers may include costs incurred during the Stop Work Order. FAR 52.216-7g, *Allowable Cost and Payment*, states, "*At any time or times before final payment, the Contracting Officer may have the Contractor's invoices or vouchers and statements of cost audited.*"

In her November 5, 2008 request, the contracting officer asked that all public vouchers on the contract be held until the matter is resolved. On January 22, 2009 in an email to the administrative contracting officer, the contracting officer wrote:

*"Please provide the status of this audit. This was supposed to be completed at the beginning of December. I cannot release any invoices until this is completed and a review is done."*

On April 30, 2009, nearly six months after receiving the request, DCAA Santa Ana Branch Office sent an email to the contracting officer to advise her of the major areas of concern. DCAA identified a significant amount of vendor and subcontractor costs included in the public vouchers that the contractor had not paid. After another four months, DCAA issued a memorandum to the contracting officer dated September 11, 2009 that canceled the review because the contractor failed to provide financial statements, tax returns, certain bank statements, and other requested supporting documents. The content of the memorandum is identical to a May 2009 draft.

We found that DCAA's failure to respond timely to the contracting officer's request for review of public vouchers hindered the contracting officer's efforts to make contractual

decisions in a timely manner or to resolve the interim public vouchers that were being held from payment.

### ***Review of Interim Public Vouchers***

We found that DCAA did not review any of the first 12 interim public vouchers that it approved for payment. If DCAA had reviewed at least one of the interim public vouchers, the Government could have stopped payments to the contractor sooner and minimized losses under the contract.

In response to the April 14, 2011 Notice of Concern, the Regional Director, DCAA Western Region stated, “The vouchers themselves, as submitted by the contractor did not indicate any significant high risk factors. The contractor provided copies of source documentation (e.g., timesheets, invoices, statement of services) for all billed costs requested on vouchers submitted in Wide Area Work Flow (WAWF). In addition, prior experience with the contractor did not indicate any systemic high risk factors that would have led to increased voucher reviews. This was not the contractor’s first contact. The Santa Ana Branch Office had processed vouchers on another contract, No. FA8718-06-C-0068 through January 2007.”

We disagree with the Regional Director’s comment that prior experience with the contractor did not indicate any systemic high risk factors that would have led to increased voucher reviews. In accordance with agency guidance, as noted below, the contractor was high risk and at least one of the interim vouchers should have been selected for review.

In accordance with DFARS 242.803(b), the contract auditor is the authorized representative of the contracting officer for receiving vouchers from contractors and approving interim vouchers for provisional payment.

We reviewed applicable DCAA procedures and guidance for reviewing interim public vouchers. DCAA guidance in CAM 6-1003f states, *“The primary purpose of the examination and approval of interim public vouchers is to provide reasonable assurance that the amounts claimed are not in excess of that which is properly due the contractor in accordance with the terms of the contract. The extent of audits of individual interim vouchers should be based upon the contractor’s integrity, its financial condition and the adequacy of its internal management controls and procedures.”*

The contractor had one previous contract awarded on September 21, 2005. DCAA performed one audit of the contractor’s accounting system. DCAA’s audit report dated November 2, 2005 stated the examination did not include tests to determine whether internal controls were in operation or operating effectively. In addition, the report stated the contractor has one government contract valued at \$763,148 but no actual sales had been recorded as of October 28, 2005.

The subject contract was awarded in June 2008. In accordance with agency guidance, DCAA should have examined an interim public voucher submitted under the June 2008 contract before approving 12 public vouchers for payment for the following reasons:

- DCAA did not perform an audit of the accounting system since 2005.
- DCAA did not determine if the contractor was financially sound.
- DCAA did not determine if the contractor's internal controls and procedures for accumulating cost and preparing public vouchers were acceptable.

Without an audit of the contractor's accounting system since 2005, at least one interim public voucher received by DCAA in 2008 should have been reviewed prior to approval for payment.

### ***Issuance of a DCAA Form 2000***

DCAA did not issue a DCAA Form 2000, "Suspected Irregularity Referral Form," even though DCAA indicated that it would do so in its September 11, 2009 memorandum to the contracting officer. DCAA found suspected irregularity during its review and drafted a DCAA Form 2000 that states:

- the contractor claimed costs on public vouchers that did not further the contracted research efforts,
- the costs relate primarily to marketing,
- a significant portion of billed costs were not actually incurred, and
- the owner and sole employee salary was billed to the government on a full-time basis with no evidence he attempted to perform meaningful research efforts under the contract.

DCAA did not follow DCAA agency guidance by not issuing a DCAA Form 2000. CAM 4-702.4, "*Procedures for Referring Suspicions*," states, upon encountering or receiving information which raises a reasonable suspicion of fraud, corruption, or unlawful activity relating to a Government contract, promptly prepare a DCAA Form 2000. Further, the guidance states that use of the DCAA Form 2000 is the preferred method for forwarding this information because the form specifies the information needed by investigators and provides for appropriate consideration of audit impact.

Submission of a DCAA Form 2000 would have assisted authorities in their investigation of the matter and facilitated the recoupment of amounts owed to the Government.

### ***Issuance of a DCAA Form 1***

DCAA did not issue a DCAA Form 1, "Notice of Contract Cost Suspended and/or Disapproved" when the auditor found that the contractor billed accrued costs that the contractor is delinquent in paying for in the ordinary course of business. The contractor did not pay his subcontractors, vendors, or other invoices that were accrued and billed to the Government on public vouchers. FAR 52.216-7, *Allowable Cost and Payment*, does not allow a contractor to bill accrued costs that the contractor is delinquent in paying for in the ordinary course of business. DFARS 242.803(b) states the auditor is the authorized

representative for issuing DCAA Forms 1 to deduct costs where allowability is questionable.

DCAA did not follow DCAA agency guidance. CAM 6-1003c states, “If the evaluation of a voucher raises a question regarding the allowability of a cost under the contract terms, the auditor, after informal discussion as appropriate, will issue a DCAA Form 1, “Notice of Contract Costs Suspended and/or Disapproved”. The DCAA Form 1 is submitted to the contractor, disbursing officer, and contracting officer. By failing to issue a DCAA Form 1, DCAA did not notify the contractor of the unallowable costs or its intent to suspend/disapprove billed costs. Timely submission of a DCAA Form 1 would have triggered the administrative contracting officer’s involvement in the process and facilitated the recoupment of amounts owed to the Government.

## **Notice of Concern, Management Comments, and Our Response**

On April 14, 2011, we issued a Notice of Concern<sup>1</sup> to the Director, DCAA to recommend corrective actions to address the reported deficiencies and to improve audit services (see Appendix B). In a June 17, 2011 response, DCAA concurred with 5 of 7 recommendations (see Appendix C). Discussed below is a summary of management comments and our response.

### ***Deleted and Renumbered Recommendations***

As a result of management comments and additional work, we deleted Notice of Concern Recommendation 6. We renumbered Notice of Concern Recommendation 7 as Recommendation 6.

The Director, DCAA disagreed with Notice of Concern Recommendation 6 that DCAA issue a report to the contracting officer to report the findings based on a review of the first 12 public vouchers that were approved for payment. The Director stated he does not believe issuing an audit report is possible or value added at this time as the issues are currently under investigation and DCAA is assisting in the investigation. After further discussion with the Contracting Officer and Attorney, Hanscom Air Force Base, we agree with the Director’s comment and deleted Notice of Concern Recommendation 6 from this report.

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<sup>1</sup> A Notice of Concern is issued to alert DOD management of significant findings that require immediate attention. By Issuing a Notice of Concern, DOD management officials can take proactive steps to mitigate the reported issue.

## ***Recommendations***

We recommend that the Director, Defense Contract Audit Agency:

- 1. Review the quality assurance procedures of the DCAA Santa Ana Branch Office for ensuring timely responses to audit requests.**

## ***Management Comments***

The Director concurred. The Director states that the Santa Ana Branch Office staff received extensive quality training over a three-day period from March 22 to 24, 2010. The Branch Office plans to provide additional training and emphasis to its staff to comply with Memorandum for Regional Directors (MRD) 10-PAS-024(R) "Rules of Engagement" issued on September 9, 2010 including issuing timely acknowledgement memos, due-date extensions, timely processes to cancel audit assignments, and timely communication throughout the audit cycle.

## ***Our Response***

The comments are responsive and no further comments are required.

- 2. Reassess the adequacy of its procedures for reviewing public vouchers.**

## ***Management Comments***

The Director concurred. By June 30, 2011, the Santa Ana Branch Office will reassess its processes and procedures for reviewing public vouchers to ensure that they are in compliance with Agency policy, risk-based, and in consideration of the DODIG findings. DCAA Policy and Plans Directorate is currently reviewing its public voucher review process and working with the Defense Procurement Acquisition Policy in revising the Wide Area Workflow to allow the DCAA public voucher review process to be more risk-based than the current process. DCAA expects the revisions to Wide Area Workflow to be completed by November 2011.

## ***Our Response***

The comments are responsive and no further comments are required.

- 3. Review the first public voucher under a new contract when audits of the accounting system, related internal controls, or public vouchers on other contracts have not been performed.**

## ***Management Comments***

The Director concurred. By November 2011, DCAA expects to issue revised policy to require DCAA auditors to review the first voucher submitted under a new contract.

## ***Our Response***

The comments are responsive and no further comments are required.

- 4. Evaluate the effectiveness of its procedures and processes for submitting a DCAA Form 2000 when the auditor suspects irregular conduct and a DCAA Form 1 when the contractor is delinquent in paying accrued costs in the ordinary course of business.**

### ***Management Comments***

The Director concurred. By August 31, 2011, the Santa Ana Branch Office will review current Agency guidance with the staff. By September 2011, DCAA will perform an assessment of current Agency policy to ensure that it appropriately addresses the necessary actions to issue a DCAA Form 1 and/or Form 2000 when it is found that the contractor is delinquent in paying accrued costs in the ordinary course of business.

### ***Our Response***

The comments are responsive and no further comments are required.

- 5. Reassess the guidance issued in the Memorandum for Regional Directors (MRD) 10-PPS-017(R) dated June 1, 2010, that authorized Regions and Field Audit Office (FAO) managers to revise their delegations of signatory authority to permit delegation to GS-9 level auditors and above with the authority to provisionally approve interim public vouchers. We recommend that delegations to GS-9 level auditors and above be granted only for financially sound contractors where audit experience indicates that contractors' internal controls and procedures for accumulating costs and preparing public vouchers are acceptable (low to moderate control risk).**

### ***Management Comments***

The Director disagreed. The Director states that the current delegation of signature authority already mandates that delegation for signing public vouchers be based on the FAO manager's discretion and will ensure that auditors' delegated approval authority possesses the necessary experience and competence to protect the Government's interest considering specific contractor risks.

### ***Our Response***

The Director's comments are not responsive. We request that the Director reconsider his position. Specifically, the Director did not comment on the recommendation that the delegation to GS-9 level auditors and above will be limited to only financially sound contractors where audit experience indicates that contractor's internal controls and procedures for accumulating costs and preparing public vouchers are acceptable. The Director states DCAA will ensure auditor's that are delegated approval authority possess the necessary experience and competence to protect the Government's interests considering specific contractor risks. We disagree. DCAA hires auditor trainees at the GS-9 level. Auditors at the GS-9 level do not possess the professional judgment or technical knowledge and competence to protect the taxpayer and Government's interests from high risk contractors that do not have approved accounting and billing systems. Therefore, we request

that the Director reconsider his position on the recommendation and provide comments in response to the final report.

**6. Review an appropriate minimum sample of previously approved vouchers to determine the extent to which these deficiencies exist with the vouchers of other DOD contractors under the cognizance of the Santa Ana Branch Office.**

***Management Comments***

The Director concurred. By December 31, 2011, the Santa Ana Branch Office will perform a review of vouchers submitted by high risk nonmajor contractors to include tests to verify that they are paying their vendors in the ordinary course of business.

***Our Response***

The comments are responsive and no further comments are required.

# **Appendix A. Scope and Methodology**

We evaluated the actions that DCAA Santa Ana Branch Office took in response to the contracting officer's request for review of the contractor's interim public vouchers. The review was conducted in accordance with the Council of the Inspectors General on Integrity and Efficiency "Quality Standards for Inspection and Evaluation." As part of our review, we:

- interviewed the contracting officer, attorney, and investigator Hanscom Air Force Base and obtained related documents;
- interviewed DCAA employees, Santa Ana Branch Office who were involved in reviewing the interim public vouchers and obtained related documents;
- reviewed applicable DCAA policies and procedures, such as the CAM; and
- reviewed applicable FAR and DFARS provisions.

We performed this review from February 2010 through May 2011.

## **Use of Computer-Processed Data**

We did not rely on any computer-processed data as part of our review.

## **Prior Coverage**

During the last 5 years, the Government Accountability Office (GAO) and the DOD IG have issued 3 reports related to audit issues at DCAA. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DOD IG reports can be accessed at <http://www.dodig.mil/audit/reports>.

### **GAO**

Report No. GAO-09-468, "DCAA Audits: Widespread Problems with Audit Quality Require Significant Reform," September 23, 2009

Report No. GAO-08-857, "DCAA Audits: Allegations That Certain Audits at Three Locations Did Not Meet Professional Standards Were Substantiated," July 22, 2008

### **DOD IG**

Report No. D-2009-6-009, "Defense Contract Audit Agency Audit Work Deficiencies and Abusive Work Environment Identified by the Government Accountability Office," August 31, 2009

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## Appendix B. DOD Inspector General Notice of Concern



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

APR 14 2011

### MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY

SUBJECT: Notice of Concern – Ineffective Audit Support Regarding a Request for Review of Public Vouchers

In our review of a Department of Defense (DOD) Hotline complaint, we identified significant concerns regarding audit support that the Defense Contract Audit Agency (DCAA), Santa Ana Branch Office, failed to provide in response to an Air Force request for a review of interim public vouchers. Our concerns address timeliness in responding to the review request, failure to select and review any interim public vouchers, failure to issue a DCAA Form 2000 for suspected irregular conduct, and failure to issue a DCAA Form 1 to suspend costs billed by a contractor that is delinquent in paying for accrued costs in the ordinary course of business.

On June 11, 2008, the Air Force awarded a cost plus fixed fee contract to Optikey LLC in the amount of \$637,990. On July 3, 2008, the contracting officer issued a Stop Work Order because the Air Force believed that the contractor did not comply with certain contract terms. While in effect, the Stop Work Order prohibited the contractor from incurring additional costs under the contract. The contracting officer lifted the Stop Work Order on September 29, 2008. On November 5, 2008, the contracting officer requested that the DCAA Santa Ana Branch Office review 12 interim public vouchers submitted by the contractor under the contract totaling \$130,119 because the contracting officer suspected the vouchers might include costs incurred during the Stop Work Order. DCAA had previously approved the 12 vouchers for payment through the Wide Area Workflow network. The contracting officer directed DCAA not to approve any further vouchers for payment pending DCAA's review of the 12 public vouchers.

In a September 11, 2009, memorandum (ten months after the contracting officer's audit request), the DCAA Santa Ana Branch Office informed the contracting officer that it was canceling the review (see attachment). The memorandum stated that a review of the public vouchers could not be performed because the contractor failed to provide financial statements, tax returns, certain bank statements, and other requested supporting documents. Nevertheless, the memorandum identified a significant amount of vendor and subcontractor costs included in the vouchers that the contractor had not paid, prompting the Santa Ana Branch Office to state that it would refer the matter to the Defense Criminal Investigative Service (DCIS). The September 11, 2009, memorandum confirmed telephone conversations that occurred on April 30, 2009, and a draft of the

memorandum dated May 2009. The content of the May 2009 draft memorandum is identical to the September 11, 2009, memorandum.

At the request of the contracting officer, an investigation was initiated by the Air Force Office of Special Investigations. The investigation confirmed that the contractor used the public voucher payments for personal purposes rather than to pay vendors and subcontractors. As a result, the Government debarred the contractor from future contract awards, and the Air Force is attempting to recover the voucher payments from the contractor.

We have four concerns regarding the audit support provided by the DCAA Santa Ana Branch Office:

1. We question why the Santa Ana Branch Office took ten months to issue the September 2009 memorandum and cancel the review when the contractor failed to provide the requested records in a timely manner. Also, we question why it took four months to issue the September 2009 memorandum which is identical to the May 2009 draft memorandum. Although the Santa Ana Branch Office provided a draft of the memorandum in May 2009, the contracting officer could not make any final contractual decisions based on the draft memorandum. We noted that the auditor made repeated, unsuccessful attempts over several months to obtain required supporting records from the contractor.
2. The Santa Ana Branch Office did not review any of the 12 public vouchers that it approved for payment under the contract. If DCAA had reviewed at least one of the public vouchers, the Government could have stopped the payments to the contractor sooner and minimized any losses under the contract. While we recognize that DCAA cannot review all of the public vouchers that it approves for payment, however, in this case, the Branch Office should have increased its scrutiny of the contractor's vouchers following an issuance of the Stop Work Order. We noted that a portion of 1 of the 12 vouchers approved by the Santa Ana Branch Office included costs that were incurred and strictly prohibited under the Stop Work Order. The contractor submitted the public vouchers under one contract and there were no current audits of the contractor's accounting or related internal control system. Therefore, minimum audit steps in the Contract Audit Manual (CAM) 6-1006 should have been performed.

We reviewed the applicable DCAA procedures for reviewing public vouchers. While CAM 6-1008 states that sampling techniques should be used to select specific vouchers for review, the procedures do not provide clear guidance on how these sampling techniques should be applied. For

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example, the procedures do not indicate whether the techniques should be applied at a DCAA office level, contractor level, or at a contract level. In addition, DCAA should consider revising its procedures to recommend a review of the first voucher received on a new contract when the contractor's accounting system, related internal controls, or prior public vouchers have not been examined.

3. Our review disclosed that the Santa Ana Branch Office did not submit a DCAA Form 2000, "Suspected Irregularity Referral Form," even though the Branch Office indicated that it would do so in its September 11, 2009, memorandum to the contracting officer. Timely submission of a DCAA Form 2000 would have assisted authorities in their investigation of the matter and facilitated the recoupment of amounts owed to the Government.
4. Our review disclosed that the Santa Ana Branch Office did not submit a DCAA Form 1, "Notice of Contract Cost Suspended and/or Disapproved" when the Branch Office found that the contractor billed accrued costs that the contractor is delinquent in paying. Federal Acquisition Regulation (FAR) 52.216-7, "Allowable Cost and Payment," clause does not allow a contractor to bill accrued costs that the contractor is delinquent in paying for in the ordinary course of business. Timely submission of a DCAA Form 1 would have triggered the administrative contracting officer's involvement in the process and facilitated the recoupment of amounts owed to the Government.

DCAA should review this matter and take appropriate corrective action to improve audit services in response to public voucher review requests. At a minimum, we recommend that DCAA:

1. review the quality assurance procedures of the DCAA Santa Ana Branch Office for ensuring timely responses to audit requests;
2. reassess the adequacy of its procedures for reviewing public vouchers;
3. review the first public voucher under a new contract when audits of the accounting system, related internal controls, or public vouchers on other contracts have not been performed;
4. evaluate the effectiveness of its procedures and processes for submitting a DCAA Form 2000 when the auditor suspects irregular conduct and a DCAA Form 1 when the contractor is delinquent in paying accrued costs in the ordinary course of business;

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5. reassess the guidance issued in the Memorandum For Regional Directors (MRD) 10-PPS-017(R) dated June 1, 2010, that authorized Regions and Field Audit Office (FAO) managers to revise their delegations of signatory authority to permit delegation to GS-9 level auditors and above with the authority to provisionally approve interim public vouchers. We recommend that delegations to GS-9 level auditors and above be granted only for financially sound contractors where audit experience indicates that contractors' internal controls and procedures for accumulating costs and preparing public vouchers are acceptable (low to moderate control risk);
6. issue a report to the contracting officer within 60 days of the issuance of this memorandum to report the findings based on a review of the first twelve public vouchers that were approved for payment as noted in the Santa Ana Branch Office September 2009 memorandum; and
7. review an appropriate minimum sample of previously approved vouchers to determine the extent to which these deficiencies exist with the vouchers of other DOD contractors under the cognizance of the Santa Ana Branch Office.

We issue a Notice of Concern to alert DOD management of significant findings requiring immediate attention. By issuing a Notice of Concern, DOD management can take proactive steps to mitigate the reported issue.

Please provide a response to our recommendations by May 20, 2011, including any planned corrective actions. If you have any questions regarding this memorandum, please contact me at (703) 604-8877 or Ms. Meredith Long-Morin at (703) 604-8739 ([meredith.morin@dodig.mil](mailto:meredith.morin@dodig.mil)).

*Carolyn R. Davis*  
Carolyn R. Davis  
Assistant Inspector General  
for Audit Policy and Oversight

Attachment:  
As stated

cc:  
Contracting Officer, Hanscom Air Force Base,

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# Appendix C. Defense Contract Audit Agency Response to Notice of Concern



DEFENSE CONTRACT AUDIT AGENCY  
DEPARTMENT OF DEFENSE  
8725 JOHN J. KINGMAN ROAD, SUITE 2135  
FORT BELVOIR, VA 22060-6219

OFFICE OF THE DIRECTOR

June 17, 2011

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL, AUDIT POLICY AND  
OVERSIGHT, OFFICE OF THE INSPECTOR GENERAL,  
DEPARTMENT OF DEFENSE

SUBJECT: Response to Department of Defense Office of Inspector General (DoDIG) Notice of Concern – Ineffective Audit Support Regarding a Request for Review of Public Vouchers, dated April 14, 2011

Thank you for the opportunity to respond to the subject review results regarding review of a Department of Defense Hotline complaint at the Defense Contract Audit Agency (DCAA), Santa Ana Branch Office (SABO). The DoDIG determined that the SABO provided inadequate audit support in response to an Air Force request for a review of interim public vouchers. The results addressed four concerns and seven associated recommendations that DCAA should review and take appropriate action to improve audit services in response to public voucher review requests.

We are providing additional factual and clarifying data for the DoDIG's consideration relating to the four concerns regarding the audit support provided by the DCAA Santa Ana Branch Office (see Enclosure).

The following are DCAA's comments and responses to each of the recommendations.

**DoDIG Recommendation 1:** DCAA review the quality assurance procedures of the DCAA Santa Ana Branch Office for ensuring timely responses to audit requests.

**DCAA Response:** Concur. The SABO has emphasized to its staff the new processes for ensuring timely responses to audit requests. The SABO received extensive quality training over a three-day period from March 22 to 24, 2010. The training covered MRD 10-PAS-024(R) "Rules of Engagement" issued on September 9, 2010. This MRD sets the ground rules that cover the timeliness of communications during the audit cycle. The SABO plans to provide additional training and emphasis to its staff to comply with the MRD, including issuing timely acknowledgement memos, timely due-date extensions, if necessary, timely processes to cancel audit assignments, and timely communication throughout the entire audit cycle.

**DoDIG Recommendation 2:** DCAA reassess the adequacy of its procedures for reviewing public vouchers.

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**SUBJECT:** Response to Department of Defense Office of Inspector General (DoDIG) Notice of Concern – Ineffective Audit Support Regarding a Request for Review of Public Vouchers, dated April 14, 2011

**DCAA Response:** Concur. By June 30, 2011, the SABO will reassess its processes and procedures for reviewing public vouchers to ensure that they are in compliance with Agency policy, risk-based and in consideration of the DoDIG findings. DCAA Policy and Plans Directorate is currently reviewing its public voucher review process. This includes working with DPAP in revising the Wide Area Workflow to allow the DCAA public voucher review process to be more risk-based than the current process. The proposed revised process will allow WAWF to identify the high risk vouchers that would require a DCAA review prior to payment. DCAA expects the revisions to Wide Area Workflow to be completed by November 2011. See the comments to Recommendation 3 for Agency policy actions on the review of the first voucher.

**DoDIG Recommendation 3:** DCAA review the first public voucher under a new contract when audits of the accounting system, related internal controls, or public vouchers on other contracts have not been performed.

**DCAA Response:** Concur. Agency policy is being revised to require DCAA auditors to review the first voucher submitted under a new contract. DCAA is working with DPAP to revise the Wide Area Workflow to require all first vouchers to be submitted to DCAA for review. We expect the deployment of this process to be completed by November 2011.

**DoDIG Recommendation 4:** DCAA evaluate the effectiveness of its procedures and processes for submitting a DCAA Form 2000 when the auditor suspects irregular conduct and a DCAA Form 1 when the contractor is delinquent in paying accrued costs in the ordinary course of business.

**DCAA Response:** Concur. The SABO will review current Agency guidance with the staff in upcoming staff conferences. We expect to complete this action by August 31, 2011. By September 2011, we will perform an assessment of current Agency policy to ensure that it appropriately addresses the necessary actions to take (i.e., issuance of a DCAA Form 1 and/or Form 2000) when it is found that the contractor is delinquent in paying accrued costs in the ordinary course of business.

**DoDIG Recommendation 5:** DCAA reassess the guidance issued in the Memorandum For Regional Directors (MRD) 10-PPS-017(R) dated June 1, 2010, that authorized Regions and Field Audit Office (FAO) managers to revise their delegation of signature authority to permit delegation to GS-9 level auditors and above with the authority to provisionally approve interim public vouchers. We recommend that delegation to GS-9 level auditors and above should be granted only for financially sound contractors where audit experience indicates that contractors' internal controls and procedures for accumulating costs and preparing public vouchers are acceptable (low to moderate risk).

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**SUBJECT:** Response to Department of Defense Office of Inspector General (DoDIG) Notice of Concern – Ineffective Audit Support Regarding a Request for Review of Public Vouchers, dated April 14, 2011

**DCAA Response:** Nonconcur. We do not believe the delegation of signatory authority is the root cause of the conditions found by the DoDIG, however, we believe the current public voucher review process may have contributed to the issues found. Therefore, as recommended by the DoDIG, DCAA will evaluate its policies and procedures for the public voucher review process, as discussed in Recommendations 2 and 3 above. The current delegation of signature authority already mandates that delegation for signing public vouchers be based on the FAO manager's discretion and will ensure that auditors' delegated approval authority possesses the necessary experience and competence to protect the Government's interests considering specific contractor risks.

**DoDIG Recommendation 6:** DCAA issue a report to the contracting officer within 60 days of the issuance of this memorandum to report the findings based on a review of the first twelve public vouchers that were approved for payment, as noted in the Santa Ana Branch Office 2009 memorandum.

**DCAA Response:** Nonconcur. We do not believe issuing an audit report is possible or value added at this time as the issues are currently under investigation and DCAA is assisting in the investigation. In addition, we do not believe the SABO was provided sufficient evidence at the time to complete the audit of the contractor's billed costs under the subject contract and issue an audit report without a disclaimer of opinion.

**DoDIG Recommendation 7:** DCAA review an appropriate minimum sample of previously approved vouchers to determine the extent to which these deficiencies exist with the vouchers of other DoD contractors under the cognizance of the Santa Ana Branch Office.

**DCAA Response:** Concur. The SABO will perform a review of vouchers submitted by high risk nonmajor contractors to include tests to verify that they are paying their vendors in their ordinary course of business. We will complete this additional testing by December 31, 2011.

Questions regarding this memorandum should be directed to the undersigned at (703) 767-3200 or Mr. Kenneth J. Saccoccia, Assistant Director, Policy and Plans Directorate, at (703) 767-3280.



Patrick J. Fitzgerald  
Director

Enclosure:  
Memorandum from Western Region



IN REPLY REFER TO

RD-4 720.1

June 16, 2011

MEMORANDUM FOR DIRECTOR, DCAA

SUBJECT: Notice of Concern, Ineffective Audit Support Regarding a Request of Review of Public Voucher

The Western Region is pleased to provide additional factual and clarifying information for consideration by the DoDIG in regards to their concerns over the audit support provided by the Santa Ana Branch Office (SABO) in support of the contracting officer's request for audit of Optikey LLC public vouchers. The additional information relates only to the four concerns cited in the DoDIG's April 14, 2011 memorandum as DCAA, HQ Policy will respond separately to the seven recommendations.

1. **Concern – Timeliness** in issuing the September 2009 memorandum that canceled the audit request while also providing information upon which the contracting officer could make final contractual decisions.

We agree the memorandum to close out the assignment was not issued timely. However, as the DoDIG notes, the SABO had disclosed its interim findings and concerns to both the ACO and PCO by April 30, 2009 and the PCO acted on this information.

The SABO received the request for audit services from the Air Force Contracting Officer through the DCMA ACO on November 5, 2008. After further discussions and coordination with the contracting officer, the SABO acknowledged the audit request on November 13, 2008. The purpose of this initial audit request was primarily to determine if unallowable costs were billed on the contract during a stop work order (SWO) period on contract FA8718-08-C-0039. The request noted that the SWO period was from July 3, 2008 through September 29, 2008; however, as discussed further below, Optikey disputed the SWO period insisting that it should only be from July 3, 2008 to September 3, 2008. The SABO kept the contracting officer well informed of the issues encountered while attempting to perform the audit. Events leading to the cancellation of the audit are as follows:

- On December 4, 2008, the auditor informed the ACO that the contractor was not supporting our audit pending consultation with its lawyers about the SWO period. On December 8, 2008, the PCO acknowledged receipt of a letter from the contractor's lawyers which advised the contractor to support the audit while they continued to dispute the SWO period.
- On April 20, 2009, approximately five months after the initial request, the contracting officer provided DCAA a copy of the contractor's final settlement claim dated April 17,

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RD-4 720.1

June 16, 2011

SUBJECT: Notice of Concern, Ineffective Audit Support Regarding a Request of Review of Public Voucher

2009 to resolve all issues in dispute with the PCO on Termination Settlement Form SF1437 (although no termination notice was issued and the period of performance had expired).

- Subsequent to receiving the contractor's April 17, 2009 final settlement claim, the contracting officer issued a new request to audit all contract costs while also providing a revised SWO period of July 3, 2008 to September 3, 2008. The SABO had a draft report prepared at this point in time based on the initial November 5, 2008 audit request, which questioned costs that were incurred during the original SWO period of July 3, 2008 to September 29, 2008. However, the SWO period noted in the second request substantially eliminated the draft question costs.
- While the issue of costs incurred during the SWO period was no longer a primary concern, the contractor's final settlement claim provided an avenue for the PCO to address other concerns with Optikey's billed contract costs. Concurrently, the SABO discussed with the contracting officer suspected irregularities in contract charges.
- In an e-mail dated April 29, 2009, the contracting officer asked for additional information to start the "OSI process". In an April 30, 2009 e-mail, the SABO informed the contracting officer of suspected irregularities in contract charges including: (i) the possible billings of unallowable costs, (ii) possible costs billed to the Government that were never paid to vendors, and (iii) lack of evidence of research effort being performed or research reports being prepared as required on the contract.
- The contracting officer took action on the information that SABO provided forwarding the allegations to AFOSI on May 13, 2009.

A draft cancellation memo was prepared on May 4, 2009, yet, as correctly noted, the final signed cancellation memo was not issued until September 1, 2009, about four months later. We agree the FAO should have issued this memorandum sooner. However, the SABO provided the relevant information to the PCO and it is clear that the contracting officer did not wait for the issuance of the September 2009 memorandum, or a DCAA Form 2000 to initiate appropriate action.

**2. Concern** – The concern states that if DCAA had reviewed at least one of the vouchers, the Government could have stopped payments to the contractor sooner and minimized losses. Further, the branch office should have increased its scrutiny of the vouchers following issuance of a stop work order.

The SABO was not able to increase surveillance of vouchers timely for unallowable costs resulting from an SWO because the ACO and DCAA were not informed of the SWO in a timely manner. The contracting officer did not inform the DCMA ACO of the SWO until a November 4, 2008 e-mail. The ACO then informed the SABO of the SWO and initiated a request for audit on November 5, 2008. DCAA did not approve any vouchers for payment subsequent to November 5, 2008.

2  
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RD-4 720.1

June 16, 2011

**SUBJECT:** Notice of Concern, Ineffective Audit Support Regarding a Request of Review of Public Voucher

The vouchers themselves, as submitted by the contractor did not indicate any significant high risk factors. The contractor provided copies of source documentation (e.g., timesheets, invoices, statement of services) for all billed costs requested on vouchers submitted in Wide Area Work Flow (WAWF). In addition, prior experience with the contractor did not indicate any systemic high risk factors that would have led to increased voucher reviews. This was not the contractor's first contract. The SABO had processed vouchers on another contract, No. FA8718-06-C-0068 through January 2007.

**3. Concern** – The Santa Ana Branch Office did not issue a DCAA Form 2000 “Suspected Irregularity Referral Form”.

We agree that a DCAA Form 2000 should have been issued during the course of the subject audit. The purpose of the DCAA Form 2000 is to alert the proper investigative group there is information that suggests a reasonable basis for suspicion of fraud, corruption, or unlawful activity affecting Government contracts. As stated above, the SABO provided the contracting officer with various concerns, including: (i) the possible billings of unallowable costs, (ii) possible costs billed to the Government that were never paid to vendors, and (iii) lack of evidence of research effort being performed or research reports being prepared as required on the contract. These issues were specifically captured in an April 30, 2009 e-mail and were substantially the same information that was included in a draft DCAA Form 2000 that was prepared, yet never issued. While a DCAA Form 2000 was not issued, the information was conveyed to the contracting officer who took quick action to forward these concerns to AFOSI.

For your information, the investigation is still in process and DCAA continues to support the investigation.

**4. Concern** – The Santa Ana Branch Office did not submit a DCAA Form 1 “Notice of Contract Cost Suspended and/or Disapproved” for subcontract and/or third party vendor costs that the contractor was delinquent in paying.

We agree that a Form 1 should have been issued notifying the contracting officer to suspend the subject costs. As noted above, the SABO provided the contracting officer with various concerns, including possible costs billed to the Government that were never paid to its vendors. An investigation is ongoing relative to these allegations.

If you have any questions or require additional information, please contact the undersigned at (714) 228-7001.

*/Signed/*  
DONALD L. MULLINAX  
Regional Director

3  
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# Inspector General Department of Defense

